



Doing Business In El Salvador: A Country Commercial Guide for U.S. Companies

Chapter 1: Doing Business In El Salvador

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Market Overview

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- The U.S.-Central American-Dominican Republic Free Trade Agreement (CAFTA-DR), entered into force March 1, 2006 between the United States and El Salvador. El Salvador was the first nation in Central America to implement the agreement. The agreement has also entered into force with Guatemala, Honduras, Nicaragua, and Dominican Republic, and is awaiting approval by Costa Rica.
- El Salvador belongs to the World Trade Organization. It has free trade agreements with Chile, Mexico, Dominican Republic, Panama, Taiwan, Colombia, and Central America. Free Trade Agreements with Canada and the European Union are under negotiation.
- Like the rest of Central America, El Salvador offers an open market for U.S. goods and services. Tariffs are relatively low and were reduced further with the implementation of CAFTA. VAT rate is 13%. There are almost no import restrictions. Standards take ISO, Colombian and Mexican and those in the U.S. as reference. Labeling and testing are not major issues.
- El Salvador has close ties to the U.S and is only a 3-4 hour flight from key U.S. gateways.
- As of December 2007, trade statistics indicated that the United States is El Salvador's leading trade partner, enjoying a 35.6% import market share. The U.S. is the destination of 50.8% of Salvadoran exports. Central America and Mexico are other top bilateral trade partners.
- Increased trade with the United States is key to further growth and development. El Salvador offers an outstanding platform for industrial and service investments aimed at re-exports.
- The Government of El Salvador (GOES) views private investment, both domestic and foreign, and increased trade as crucial to development.
- The government has a marginal role in the economy due to privatizations that began in 1990.

- El Salvador has the most open trade and investment environment in Central America and is surpassed in Latin America only by Chile, according to the Heritage Index of Economic Freedoms. In 2008 El Salvador was ranked 33 at 69.2 percent, “moderately free,” out of 162 countries (see <http://www.heritage.org/research/features/index/countries.cfm>).
- Transparency International Corruption Perception 2007 Index ranked El Salvador 67 out of 179 countries (see http://www.transparency.org/policy_research/surveys_indices/cpi/2007).
- The U.S. dollar is the official currency. El Salvador enjoys excellent macroeconomic stability, low inflation, and one of the lowest interest rates in Latin America.
- Per capita income has risen during the last decade. Consumer demand is fueled both by the increase in income and the massive inflow of remittances from Salvadorans living in the United States.
- More than 2.5 million Salvadorans live in the U.S. The most outstanding feature of El Salvador's balance of payments is the country's dependence on remittances, by far the largest source of foreign income. In 2007, remittances reached \$3.6 billion, up from \$3.3 billion in 2006.
- El Salvador enjoys a democratically elected government and has an excellent relationship with the United States. Most Salvadorans view the United States favorably.

Market Challenges

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U.S. firms need to be aware of certain challenges, including the following:

- The judicial system presents significant hurdles for U.S. companies. The system is slow and tends to favor national interests. Attempts at establishing commercial arbitration have not been supported by the judiciary.
- IPR protection is in its early stages and making progress.
- The expiration of the Multi Fiber Arrangement (MFA) at the end of 2004 caused dislocations and disinvestments in El Salvador's textile maquiladora sector. In contrast, the most efficient and largest companies in the sector are expanding by vertical integration. Investment decisions from foreign textile mills and textile finishing companies are moving forward.
- Under the electricity sector law approved in April 2003, the government can influence the retail price of electricity. This adversely affects potential investors in the sector.
- Although the National Civil Police force has improved, high levels of crime add measurably to the cost of business operations.
- Low levels of literacy and of English as a Second Language are long-term drags on economic development.

Market Opportunities

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El Salvador offers a steady and growing market for a wide range of U.S. goods and services. U.S. companies exporting to Mexico under NAFTA are well positioned to increase exports by taking advantage of CAFTA. Best prospects include:

- Automotive Parts and Service Equipment
- Dental Equipment
- Printing and Graphics
- Travel and Tourism

Major Projects Include:

- La Union Port construction and other projects related to a possible dry canal
- Rehabilitation of railroad
- Renewable-energy generation of electricity
- Regional electric grid interconnection
- Regional telecommunications interconnection
- Regional Highway interconnection
- \$461 million investments in education, public services, enterprise development, and transportation infrastructure projects funded by the Millennium Challenge Corporation (learn more in chapter 7).

Major projects are generally financed with funds from Inter-American Development Bank (IDB), Central America Bank for Economic Integration (CABEI) and Millennium Challenge Corporation.

Market Entry Strategy

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- The use of agents and distributors is the most common way to export U.S products and services.
- One agent is sufficient as commercial activity is concentrated in the capital San Salvador and the size of the country does not justify regional agents.
- Agent or representative agreements should be non-exclusive. An exclusive territorial contract is recommended only when the business relationship has proven to be stable, professional, and profitable for both parties. An exclusive agent is entitled to compensation for damages upon termination of the relationship. A local lawyer should be consulted.
- U.S. companies should visit potential partners or agents prior entering into a relationship.
- U.S. firms should check the bona fides of potential partners as soon as a business relationship begins to develop.

U.S. exporters seeking general export information/assistance or country-specific commercial information should consult with their nearest **U.S. Export Assistance Center** or the **U.S. Department of Commerce's Trade Information Center** at **(800) USA-TRADE**, or go to the following website: <http://www.export.gov>.

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